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No. 165

In the Supreme Court of the United States

OCTOBER TERM, 1960

ESTATE OF JOHN SCHLOSSER, DECEASED,
RAYMOND SCHLOSSER, EXECUTOR, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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OPINIONS BELOW

The opinion of the Tax Court (Pet. 1a–14a) is reported at 32 T.C. 262. The opinion of the court of appeals (Pet. 15a–19a) is reported at 277 F. 2d 268.

JURISDICTION

The judgment of the court of appeals was entered on March 30, 1960 (Pet. 20a). The petition for a writ of certiorari was filed on June 22, 1960. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Where the executor elected to value the decedent's estate as of the optional valuation date (one year after date of death), and in that one-year period the estate

received a stock dividend on shares owned by the decedent at death (which stock dividend was not taxable as income to the estate), is the stock dividend includible in the value of the estate determined as of the optional valuation date?

STATUTE, REGULATIONS, AND RULING INVOLVED

The pertinent portions of Section 811(j) of the Internal Revenue Code of 1939, Sections 81.10(a) and (c) and 81.11 of Treasury Regulations 105, and Revenue Ruling 58–576 are set forth in the Appendix, *infra*, pp. 7–11.

STATEMENT

The undisputed facts may be summarized as follows:

John Schlosser died on January 25, 1953, and the executor of his estate, Raymond Schlosser, elected to have the gross estate valued as of January 25, 1954, one year later, as authorized by Section 811(j) of the Internal Revenue Code of 1939 (Pet. 2a–3a). At his death, decedent owned 10,394 shares of common stock of the Sun Oil Company, a New Jersey corporation (Pet. 3a). In October 1953, the company resolved to issue an eight per cent stock dividend of common stock on the company's common stock of record at the close of business on November 13, 1953 (Pet. 3a–4a). The dividend was issued on December 15, 1953, the estate receiving 831 shares (Pet. 2a, 4a). The Commissioner included the value of these shares, as of the optional date, in the gross estate, resulting in a deficiency in estate tax of $21,150 (Pet. 2a). While the Sun Oil Company also paid cash dividends in 1953, the Commissioner did not attempt to include them as

a part of decedent's estate as of the optional valuation date (Pet. 8a).

The Tax Court sustained the Commissioner (Pet. 14a), and the Court of Appeals for the Third Circuit affirmed (Pet. 20a).

ARGUMENT

1. If an estate uses the optional valuation date, the estate does not include *cash* dividends received by it during the interim year. Since the cash dividends are subject to the income tax, this Court decided that, absent unequivocal intent by Congress to tax them twice, they would be excluded from the estate. *Maass* v. *Higgins*, 312 U.S. 443, 449; see 2 Paul, *Federal Estate and Gift Taxation*, § 18.47. But since a true stock dividend is not income (*Eisner* v. *Macomber*, 252 U.S. 189, 203, 211),[1] the estate was not subject to the income tax on the stock dividend which it received during the year after decedent's death. Thus, the taxpayer is in effect urging that it should not have to pay either an income or estate tax; instead of being taxed twice, it seeks not to be taxed at all. Since no such result was intended by the statute, the courts below correctly found the stock dividend to be subject to the estate tax.

Congress enacted the optional valuation date provision so as "to mitigate the hardship consequent upon shrinkage in the value of estates during the

[1] Although certain stock dividends give rise to income (*Koshland* v. *Helvering*, 298 U.S. 441; see *Helvering* v. *Sprouse*, 318 U.S. 604, 607), a true stock dividend, like the one here, does not do so, "chiefly for the reason that income ha[s] not been severed from capital or realized by such a distribution" (*Helvering* v. *Griffiths*, 318 U.S. 371, 373). And see Section 305 of the Internal Revenue Code of 1954 (26 U.S.C. 305).

year following death." *Maass* v. *Higgins, supra,* 312 U.S. at 446. Thus, where there was a shrinkage in value, the estate tax could be decreased by using the optional valuation date. But no such shrinkage is present here—the executor simply erred when he thought he could minimize the tax by using the optional valuation date. Instead of the decedent's interest in Sun Oil Company having shrunk in size, it had increased by 831 shares, the stock dividend, while remaining proportionately the same.

This Court has repeatedly held that a true stock dividend does not really add anything to nor take anything from the original stock because there has been no severance of income from capital. *Towne* v. *Eisner,* 245 U.S. 418, 426; *Peabody* v. *Eisner,* 247 U.S. 347, 349; *Eisner* v. *Macomber,* 252 U.S. 189; *Helvering* v. *Griffiths,* 318 U.S. 371. The stock dividend "merely changed the form of the estate's investment in the corporate stocks by increasing the number of its shares, but left the aggregate value of all its shares the same as that before the dividend shares were issued." *McDonald* v. *Maxwell,* 274 U.S. 91, 98. Thus, to reflect the fact that decedent's interest in Sun Oil Company was still proportionately the same as at the time of his death, the aggregate value of all the shares had to be counted, including the stock dividend shares. Cf. *Gibbons* v. *Mahon,* 136 U.S. 549.

2. The decision of the court of appeals is in accord both with the Regulations and with subsequent administrative interpretation of them. Although the Treasury had previously taken the view that cash dividends were taxable both as part of the estate and also as income (Regulations 80 (1937 ed.), Art. 11),

after this Court's decision in *Maass* v. *Higgins, supra,* the Treasury Regulations were amended in 1941 to preclude double taxation. T. D. 5047, 1941–1 Cum. Bull. 425. This revised provision is present in the Regulations involved here. Treasury Regulations 105, Sec. 81.11, Appendix, *infra,* p. 10. As the court of appeals held, these Regulations exclude from the estate only such dividends (whether cash or stock) as constitute income and are taxable as such to the recipient (Pet. 18a–19a).[2] And similarly Revenue Ruling 58–576, 1958–2 Cum. Bull. 625, states that "A stock dividend which is not income * * * received subsequent to the decedent's death must be included in the gross estate * * *. The declaration of the stock dividend after the decedent's death directly affects the value of the shares of stock at the subsequent valuation date so that the decedent's shares of stock * * at the subsequent valuation date no longer reasonably represent the same property interest in the corporation possessed by the decedent at the time of his death."

3. There is no conflict of decisions. Since the promulgation of the 1941 regulation, this is apparently the only reported case involving the includibility of a stock dividend received after the decedent's death in an estate valued at the optional date. While the taxpayer urges (Pet. 7-8) that the instant case is in

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[2] "To be excluded under that regulation dividends must be both 'ordinary' and 'out of earnings and profits', a description which aptly describes only such distributions as would constitute income to the recipient. The normal cash dividend is of the described type. So are stock dividends which change the stockholder's proportionate interest in the corporation or give him something different in kind from his original stock."

conflict with *McGehee* v. *Commissioner*, 260 F. 2d 818 (C.A. 5), there Section 811(j) was not concerned at all; the issue was the valuation of gifts made in contemplation of death which are includible in the gross estate under Section 811(c). Moreover, the court of appeals in *McGehee* made clear that it was of crucial importance that, as the parties had stipulated, no cash dividends were paid after the gifts, and the stock dividends represented a capitalization of income earned subsequent to the gifts. In contrast, here, the record shows that the Sun Oil Company paid both stock and cash dividends and that the stock dividend was not in entirety a capitalization of income earned after the date of decedent's death (Pet. 16a–17a). But, if, as taxpayer seems to contend (Pet. 8), *McGehee* stands for the general proposition that a true stock dividend represents something new and different from the original stock, it is in conflict with controlling decisions of this Court (see *supra*, p. 4) and is therefore clearly erroneous.

CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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APPENDIX

Internal Revenue Code of 1939:

SEC. 811. GROSS ESTATE.

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property * * *

* * * * *

(j) *Optional Valuation.*—If the executor so elects upon his return (if filed within the time prescribed by law or prescribed by the Commissioner in pursuance of law), the value of the gross estate shall be determined by valuing all the property included therein on the date of the decedent's death as of the date one year after the decedent's death, except that (1) property included in the gross estate on the date of death and, within one year after the decedent's death, distributed by the executor (or, in the case of property included in the gross estate under subsection (e), (d), or (f) of this section, distributed by the trustee under the instrument of transfer), or sold, exchanged, or otherwise disposed of, shall be included at its value as of the time of such distribution, sale, exchange, or other disposition, whichever first occurs, instead of its value as of the date one year after the decedent's death, and (2) any interest or estate which is affected by mere lapse of time shall be included at its value as of the time of death (instead of the later date) with adjustment for any difference in its value as of the later date not due to mere lapse of time. No deduction under this subchapter of any item shall be allowed if allowance for such item is in effect given by the valuation under this subsection. Wherever in any other subsection or section of this chapter, reference is made to

the value of property at the time of decedent's death, such reference shall be deemed to refer to the value of such property used in determining the value of the gross estate. * * *

* * * * *

(26 U.S.C. (1952 ed.) 811)

Treasury Regulations 105, promulgated under the Internal Revenue Code of 1939:

SEC. 81.10 *Valuation of Property.*—(a) *General*—The value of every item of property includible in the gross estate is the fair market value thereof at the time of the decedent's death; or, if the executor elects in accordance with the provisions of section 81.11, it is the fair market value thereof at the date therein prescribed or such value adjusted as therein set forth. * * * Such value is to be determined by ascertaining as a basis the fair market value as of the applicable valuation date of each unit of the property. For example, in the case of shares of stock or bonds, such unit of property is a share or a bond. All relevant facts and elements of value as of the applicable valuation date should be considered in every case.

* * * * *

(c) *Stocks and bonds.*—The value of stocks and bonds, within the meaning of the Internal Revenue Code, is the fair market value per share or bond on the applicable valuation date.

In the case of stocks and bonds listed on a stock exchange the mean between the highest and lowest quoted selling prices on the valuation date shall be considered as the fair market value per share or bond. * * *

* * * * *

SEC. 81.11. *Optional Valuation Date.*—In general, the object of subsection (j) of section 811 is to make provision whereby the amount of tax otherwise payable may be lessened when, within the year following the decedent's death,

the gross estate has suffered a shrinkage in its aggregate value.

The executor may, by an election upon his return, Form 706, if filed with the time prescribed by law or prescribed by the Commissioner in pursuance of law, have the property which was included in the gross estate on the date of the decedent's death valued as of the applicable dates, as follows:

* * * * *

(b) Any property not distributed, sold, exchanged, or otherwise disposed of within such 1-year period, valued as of the date one year after the date of decedent's death;

In valuing the gross estate under the optional valuation method, all of the property interests existing at the date of death which are a part of the gross estate as determined under subsections of section 811 constitute the property to be valued as of one year after the date of the decedent's death, or as of the date of the decedent's death, or as of some intermediate date. Such property is herein referred to as "included property." "Included property" as of the date of the decedent's death remains "included property" for the purpose of valuing the gross estate under the optional valuation method even though it is changed in form during the optional valuation period by being actually received, or disposed of, in whole or in part, by the estate. However, property earned or accrued (whether received or not) after the decedent's death and during the optional valuation period with respect to any property interest existing at the date of death, which does not represent a form of "included property" itself or the receipt thereof, is to be excluded in valuing the gross estate at the subsequent valuation date and is hereinafter referred to as "excluded property." Among

the items of "included property" to be valued in accordance with these principles are the following:

* * * * *

(4) *Stock of a corporation.*—Shares of stock in a corporation and dividends declared to stockholders of record on or before the date of the decedent's death and not collected at the date of death constitute "included property" of the estate. Ordinary dividends out of earnings and profits, whether in cash or in shares of the corporation or in other property, declared to stockholders of record after the date of the decedent's death are "excluded property" and are not to be valued under the optional valuation method. If, however, dividends are declared to stockholders of record after the date of the decedent's death with the effect that the shares of stock at the subsequent valuation date do not reasonably represent the same "included property" of the gross estate as existed at the date of the decedent's death, such dividends are "included property" except to the extent that such dividends are out of earnings of the corporation after the date of the decedent's death. For example, if a corporation makes a distribution in complete or partial liquidation to stockholders of record during the optional valuation period, the amount of such distribution received on stock included in the gross estate is itself "included property," except to the extent that the distribution was out of earnings and profits since the date of the decedent's death. * * *

* * * * *

Rev. Rul. 58–576, 1958–2 Cum. Bull. 625:

Advice has been requested with respect to the valuation to be used in certain situations where the alternate valuation method is elected pursuant to section 2032 of the Internal Revenue Code of 1954.

* * * * *

Situation No. 3.

Additional stock received as a result of a stock dividend before the year expires, but after the death of the decedent.

Answer.

A stock dividend which is not income within the meaning of the Sixteenth Amendment to the Constitution received subsequent to the decedent's death must be included in the gross estate where the alternate valuation method has been elected. The declaration of the stock dividend after the decedent's death directly affects the value of the shares of stock at the subsequent valuation date so that the decedent's shares of stock in the corporation at the subsequent valuation date no longer reasonably represent the same property interest in the corporation possessed by the decedent at the time of his death. Such a dividend is "included property" as that term is defined in section 20.2032–1 of the regulations.

* * * * * *